

Investing Suggestions to Build a Comfortable Retirement

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Dedication: To Clay, Patrick, and Mary who have taught me and thousands of educators how to invest wisely and provide for their families, communities, and charities.

Disclaimer: This handout describes personal opinions and lessons learned by David Arendale on his own journey of learning about investments. You are strongly encouraged to consult with a qualified and trained financial planner, financial investment salesperson, or other professional before making decisions.

Some Characteristics About American Millionaires (Stanley & Danko, 1996):

- ◆ More than 80 percent are ordinary people who have accumulated their wealth in one generation. The average age of achieving assets of \$1,000,000 was more than 51.
- ◆ Earning a high annual salary and spending a great deal of money is much easier than accumulating wealth. Our consumption-oriented society encourages many to engage in *conspicuous spending* rather than *prodigious saving*.
- ◆ Building wealth takes discipline, sacrifice, and hard work.
- ◆ Two-thirds of the millionaires are self-employed and operate dull/normal businesses (e.g., pest controllers, plumbers, janitorial services contractor, meat processor, mobile-home park owner) and work an average of 45 to 55 hours each week.
- ◆ The *personal character of the business owner* is more important in predicting his or her level of wealth than the classification or type of business.
- ◆ The average taxable annual family income is \$131,000.
- ◆ Nearly all own stocks and mutual funds. They tend to “buy and hold” these assets for long periods. More than 40 percent report that they did not trade any stock in the previous year. (Women generally do better in the stock market since they sell less often than men. Research suggests holding onto quality investments earns more money than frequent trading looking for “better” investments.)
- ◆ They spend about eight hours each month learning about financial principles (e.g., listening to financial radio shows, reading magazine articles, surfing to Internet sites)
- ◆ About half have lived in the same home for 20 years and most live in neighborhoods of more modest income and savings. Most millionaires do not purchase a home that requires a mortgage that is more than twice the total household’s annual income.
- ◆ The average automobile owned is either a Ford Explorer or Ford 150 Pickup Truck.
- ◆ Many millionaires buy their clothes at Penny’s and Sears.
- ◆ Millionaires maintain their affluent status the same way that they acquired it, they carefully budget and control expenses.
- ◆ There is a *negative* relationship between accumulating wealth and completing an advanced college degree. This is due to several factors: delaying entry into the

workforce for four to eight years and therefore not accumulating any wealth for that period; accumulating debt from the college education; acquiring a desire to spend money on a lifestyle that the chosen occupation cannot support.

- ◆ The more dollars adult children receive from their millionaire parents, the fewer dollars they themselves will accumulate, while those who are given fewer dollars by their parents actually accumulate more. However, paying for the education of children and other relatives does not have a direct negative effect upon them.

Seven Common Denominators Among Millionaires (Stanley & Danko, 1996):

1. They live well below their means. They are prodigious savers and investors.
2. They allocate their time, energy, and money efficiently, in ways conducive to building wealth.
3. They believe that financial independence is more important than displaying high social status.
4. Their parents did not provide economic outpatient care (e.g., no home down payments or large financial gifts). The only exception is that many parents paid for the college education of their children, grandchildren, or other relatives.
5. Their adult children are economically self-sufficient.
6. They are proficient in targeting market opportunities.
7. They chose the right occupation (e.g., self-employed).

Suggested Action Steps:

1. ***Watch the winners and imitate them.*** Observe what rich people do and adopt some of their strategies for acquiring wealth.
2. ***Have written goals.*** Commit to paper a clearly defined list of monthly, annual, and lifetime goals. (Less than 2 percent of Americans have any written goals, financial or otherwise). Post it in a place where you will see it frequently. Update as needed.
3. ***Live by a budget.*** Create a family budget and live by it. Track all expenses and income. This will help identify that indeed there is some additional money that can be invested on a regular monthly basis.
4. ***Continue to learn.*** Continually educate yourself about financial principles. Spend two hours each week listening to financial radio/television shows, reading articles, and surfing the Internet web pages. Warren Buffett, one of the world's richest men, talks about "investing in a *circle of competence*." He encourages people to select investments that they understand. The average person can sometimes do as well as the professional investor if they do their homework by continuing to learn.
5. ***Receive wise counsel.*** Invest several hundred dollars to a financial planner to help with developing a plan. They have no personal stake in whom you invest

with. Carefully select one that is endorsed by happy customers or an accountant that you trust.

6. ***Develop an independent retirement fund.*** The free retirement plan of the University is excellent. Regardless of what we may read or hear, the politicians in Washington, D.C. will keep Social Security and Medicare going strong. But the unexpected can happen and not all of us will retire from UMKC. Besides, an independent plan may provide more money than the other two retirement programs combined. Make your money work harder for you than what you had to do to earn it to begin with. While no one knows the future, it is certain that if you fail to save now you may have little later. Understanding that investing works over the long-term, you can better withstand the dramatic variations of the investments along the way.
7. ***Pay yourself first each month.*** Invest on a monthly basis. If you wait until you have paid all your bills and purchased everything that you and the family “want”, there will never be much left over to save or invest. Waiting until year’s end is difficult as well. Small sacrifices now will lead to great dividends later. Another way to think about the priorities is this way: the first fruits of all investments and income is to be first devoted to a higher calling (God, charity, and others). Second, pay yourself by investing for the future. Third, pay your monthly obligations and bills.
8. ***Don’t retire old debt with new money.*** Be careful about using current cash to pay off old debt. It is generally best to invest money in quality investments (e.g., mutual funds) than to pay down on house debt. Since the federal government permits deducting home mortgage interest costs, the “*real interest rate*” for the mortgage is generally only two-thirds of the interest rate (i.e., a seven percent mortgage is really only about five percent when considering the tax deduction for the mortgage interest). The question is, can you select an investment that will earn more than the five percent on the home mortgage?
9. ***Invest in mutual funds.*** Rather than investing in an individual stock (e.g., General Motors or IBM), a mutual fund is a collection of stocks of individual companies. Often the collection of stocks are often related to each other (e.g., technology, medical, manufacturing). These mutual funds do not increase or decrease in value as dramatically as an individual stock may. Effective fund managers buy and sell the individual stocks in their mutual fund basket depending upon their professional judgement or whether their value will go up for the short or long-term. Investing in mutual funds is a better investment than whole life insurance. Purchase much less expensive term life insurance instead. Invest the difference in cost between term and whole life in a mutual fund.
10. ***Don’t be satisfied with “average”.*** Some investment counselors suggest that investors should be happy to receive an average growth of eight percent for their money. While it does not seem to be much difference between a few

percentage points, remember the “*Rule of 72*”. For example, assume that your investment is earning an average of eight percent annually. Dividing eight into 72 is nine. This is the number of years that it will take for compounding interest growth to double your money.

Likelihood of Long-Term Annual Percentage Growth of Mutual Fund Investments

Annual Percentage	Chance of Occurring	Comments
8%	Conservative	This rate is what most experts expect.
11%	Reasonable	This is the historic rate of growth for all sectors of the New York Stock Market for the past one hundred years.
15%	Optimistic to Very Optimistic	This is the rate of most of the better aggressive mutual funds.
19%	Optimistic	A rate for aggressive mutual funds that carry high risk and volatility of value..

11. **Invest in tax-deferred mutual funds.** This will help to minimize your taxable income since the money invested is not subject to income tax. Uncle Sam is your unseen partner in investment. If you invest \$2,000 a year, the monthly investment would be \$166. But the investment really does not cost you \$166. If you had chosen to not invest, you probably would have paid \$50 to \$60 in taxes on the \$166 of income, depending upon the tax bracket that you are in. So, while you are putting in about \$116, Uncle Sam contributes the \$50 of tax that it would have received. What a deal! In addition, your investment will grow without paying taxes on its growth. Only when you begin to withdraw the money will income tax be paid. By then, you will probably be in a lower tax bracket. It is possible to some experts that in the next 20 years the government may replace the income tax with a sales tax.

Retirement Fund: Begin with \$2,000 Initial Deposit, Add \$2,000 Each Year

Compound Interest Rate	Doubling Time for Money Invested	5 Years (\$12,000)	10 Years (\$22,000)	15 Years (\$32,000)	20 Years (\$42,000)	25 Years (\$52,000)	30 Years (\$62,000)
8%	9 Years	\$14,672	\$33,291	\$60,649	\$100,846	\$159,909	\$246,692
11%	6.6 Years	\$15,826	\$39,123	\$78,380	\$144,530	\$255,998	\$443,826
15%	4.8 Years	\$17,507	\$48,699	\$111,435	\$237,620	\$491,424	\$1,001,914
19%	3.8 Years	\$19,366	\$60,807	\$159,700	\$395,695	\$958,861	\$2,302,775
24%	3.0 Years	\$21,960	\$80,476	\$252,022	\$754,930	\$2,229,267	\$6,551,473

12. **Invest in a Roth Individual Retirement Account mutual fund.** Unlike the tax-deferred mutual fund, the Roth IRA requires the investor to use money that has already been subject to income tax. However, when the money is withdrawn in the

future, it is NOT subject to income tax. Like a regular tax-deferred mutual fund, all the growth of the money along the way is not taxed. There are some other advantages to the Roth IRA in comparison to a tax-deferred one. See your financial counselor for guidance.

13. **Invest regularly.** Use payroll deduction to have the same amount of money deducted from your paycheck for investment in a mutual fund. This is called “*dollar-cost averaging*.” When the price is low, you will purchase more shares. When the price is higher, you purchase less shares but your overall financial account is therefore worth more. When possible, select “no-load” mutual funds that do not charge you fees before they invest your funds. All funds will charge small annual service fees.
14. **Invest with the best.** Carefully select mutual funds that have a high historic rate of annual growth. Not all funds are alike. With the explosive growth of the stock market in recent years, sometimes the advertising is difficult to read. Generally do not pay much attention to rate growth during the last one to three years since many funds have done well. Look for the average rate of growth during the past ten years or “since inception”, the year that the fund was established. Read the “prospectus”, the official pamphlet provided by the company that provides detailed information about the fund. It should provide a year-by-year growth of the fund. Watch for a positive annual average.
15. **Understand your current retirement benefits from your employer and Social Security.** Visit with representatives from your employer’s Human Resources. The main web page for the Social Security Administration is <http://www.ssa.gov/> The request for a report is made on the following page: <https://s00dace.ssa.gov/pro/batch-pebesbp-7004home.shtml>
16. **Upon retirement from your employer, roll a portion of your employer-provided retirement fund to another place.** Sometimes a portion of the employer retirement fund can be moved out of their retirement plan to a place of your choice. While this will reduce your monthly retirement check from the employer, it provides two advantages: (1) you can place the money in another place that will earn you more money; (2) your estate keeps that money when you die. Otherwise, your employer will keep it.
17. **Consider moving your current retirement investments to higher productive ones.** As described earlier, an improvement of a few percentage points over a long period of time can lead to dramatic changes. See the following example.

Retirement Fund With an Initial Investment of \$25,000. (No additional deposits.)

Compound Interest Rate	Doubling Time for Money Invested	5 Years	10 Years	15 Years	20 Years	25 Years	30 Years
8%	9 Years	\$36,733	\$53,973	\$79,304	\$116,524	\$171,212	\$251,566
11%	6.6 Years	\$42,126	\$70,986	\$119,615	\$201,558	\$339,637	\$572,307
15%	4.3 Years	\$50,284	\$101,139	\$203,427	\$409,163	\$822,974	\$1,655,294
19%	3.8 Years	\$59,659	\$142,367	\$339,738	\$810,736	\$1,934,701	\$4,616,883
24%	3.0 Years	\$73,291	\$214,861	\$629,891	\$1,846,603	\$5,413,550	\$15,870,503

18. **Watch your mutual fund manager.** Like in any business, people change jobs. If the fund manager in charge of the individual fund leaves the company, reconsider staying with the current fund or following the manager to the new mutual fund. Sometimes the new people do as well, or better than the original fund manager. Sometimes not.
19. **Protect your money from Uncle Sam and “death taxes”.** Invest the time and money to develop a “trust” to avoid estate taxes. The rich people have used trusts to protect their money so that they can direct it to children, family members, and charities.
20. **Keeping looking for the “new” cheese.** As popularized in Spencer Johnson’s book, *Who moved the cheese?*, those who successfully deal with change will succeed. Many of the book’s sayings apply well to discovering new investments and where they are located: “Smell the cheese often so you know when it is getting old.” “The quicker you let go of old cheese, the sooner you can enjoy new cheese.” “Move with the cheese.” “They keep moving the cheese.” Investment strategies that worked with our parents’ generation (e.g., Treasury bills, savings bonds, certificates of deposit) will never earn the sort of return that investments in aggressive mutual funds can bring. Relying on the old investment methods will eventually lead to disappointment and lost opportunities. Finding the “new cheese” will require constant vigilance and education for the investor.
21. **If you have money to “fix” a problem, you don’t have a problem.** Careful investing not only can prepare for long-term retirement, but some investments can be used earlier without penalty to pay for college education of children, first-time home ownership, and payment of catastrophic health care costs. Even if you have to pay the penalty for early use of the money (generally a ten percent penalty plus payment of income tax on tax-deferred investments), resources will be available for the unexpected.
22. **Leave a legacy for your family, community, and cause. (Covey, Merrill, & Merrill, 1994)** Between \$41 and \$136 trillion dollars will be transferred from one generation of

Americans to the next over the next 50 years. Careful planning and use of wills and trusts can help be sure that most of this money goes to productive use rather than giving it back to the federal and state government in death and estate taxes. While all of us have a limited number of days on this earth, we all have an opportunity to leave behind a lasting legacy through the investments that we have made by using those funds to help and influence others. Opportunities abound for use of the money not needed for a comfortable retirement: supplementing retirement expenses of parents, payment for college education of family members, help with first-time home purchases, gifts to charities, establishment of scholarship funds, and many more. Just as there has been considerable recent attention paid to the contributions of the World War II generation to American society, there will be many chronicles of the philanthropic activities of this generation of Americans as they give tens of trillions of dollars of gifts for the benefit of others in society for future generations.

References:

Books:

- Covey, Stephen R. (1989). *The seven habits of highly effective people: Powerful lessons in personal change*. New York: Simon & Schuster
- Covey, Stephen R., Merrill, A. Roger; & Merrill, Rebecca R. (1994). *First things first: To live, to love, to learn, to leave a legacy*. New York: Simon & Schuster
- Johnson, Spencer. (1998). *Who moved my cheese? An a-mazing way to deal with change in your work and in your life*. New York: G. P. Putnam's Sons
- Stanley, Thomas J; & Danko, William D. (1996). *The millionaire next door: The surprising secrets of America's wealthy*. New York: Pocket Books

Financial Magazines (Some provide free web sites as well):

- Family Money Magazine
- Money Magazine, <http://www.money.com/money/>
- Mutual Fund Magazine, <http://www.mfmag.com/>

Internet Web Pages

- CBS Marketwatch (free), <http://www.cbs.marketwatch.com> Great news and links
- CNBC.com (free), <http://www.CNBC.com> Great news and links
- DirectAdvice.com (\$79/year), <http://www.directadvice.com> Provides models to estimate your needs and different approaches for achieving your financial goals
- Mutual Funds Online (free for basic, \$10/month for advanced services), <http://www.mfmag.com> Plenty of links to information on mutual funds
- TheStreet.com (free), <http://www.thestreet.com> Great news and links
- Wall Street Journal Interactive (\$59/annual fee), <http://www.wsj.com> Great news and analysis. Provides much of the information available through the print publication.
- Yahoo (free), <http://www.quote.yahoo.com> Great news and links. Set up your own monitor of your stocks and mutual funds.

Daily and Weekly Television Programs:

- Wall Street Week, Public Television
- Bloomberg's Morning Business, Public Television
- Evening Business Report, Public Television
- Moneyline, Weekdays, CNN Cable Television